

Grand City Properties S.A.

Luxembourg / Real Estate
 Frankfurt
 Bloomberg: GYC GR
 ISIN: LU0775917882

Q3/22
 Results

RATING
BUY

PRICE TARGET
€ 16.80

Return Potential 59.8%
 Risk Rating Medium

CAUTIOUS MARKET OUTLOOK AFTER STABLE Q3

Nine month reporting was close to FBe and has Grand City on pace to achieve confirmed 2022 guidance. Management sounded a cautious tone on the earnings call with the impact of macro headwinds becoming more visible. At the same time, Grand City's top brass were confident in the landlord's ability to absorb the current market disruption without compromising the capital structure, even if earnings (FFO 1) take a hit over the near term. We have recalibrated our forecasts that now consider the more cautious market outlook. This points to a target price of €16.8 (old: €19). Our rating remains Buy.

Conference call takeaways Management noted that the transaction market is currently frozen, which is starting to hurt residential valuations. About 20% of the GCP portfolio will be reassessed in Q4, and we could see some pressure on valuations for the period. The company puts mid-term risk to property values at around minus 5%, which we now factor into our model. Meanwhile, GCP has provisioned €10m for rent collections as a precaution assuming that soaring energy bills will compromise household budgets. The company also believes LFL rental income growth will be flat in 2023. That being said, management are confident the balance sheet can absorb this downturn without jeopardising covenants, thanks to ample headroom and good debt coverage metrics (see note of 12 October 2022). The dividend policy remains intact for now (75% of FFO 1), but the company will make a final decision on the 2022 earnings payout just before the proposal to the AGM.

Investors need to be patient Given the fiendishly challenging macro environment, it was only a matter of time before market headwinds impacted operations. However, we remain upbeat that the landlord can batten down the hatches to ride out the storm and see good value in the GCP stock after sharp declines (-50% YTD). It is difficult to predict when property stocks might trough, but the rebound potential is good once the macro environment stabilises, as evidenced by the sharp sector rally on the back of America's last CPI report.

FINANCIAL HISTORY & PROJECTIONS

	2018	2019	2020	2021	2022E	2023E
Rental income (€m)	544.98	560.30	535.42	524.63	540.43	581.50
Y/Y growth	10.1%	2.8%	-4.4%	-2.0%	3.0%	7.6%
Adj. EBITDA (€m)	275.53	297.66	299.78	298.59	302.72	298.47
Net income (€m)	488.6	406.9	362.2	523.5	282.9	-8.6
EPRA NTA (€m)	0.00	4,357.72	4,566.43	5,020.19	5,291.08	5,097.14
EPRA NTAPS (€)	0.00	25.93	26.55	30.40	30.70	29.57
DPS (€)	0.77	0.82	0.82	0.83	0.86	0.78
FFO 1* (€m)	167.59	178.97	182.21	186.33	193.93	178.72
FFOPS 1* (€)	1.01	1.07	1.07	1.11	1.15	1.04
Liquid assets (€m)	765.04	1,069.46	1,697.91	1,113.53	556.89	640.68

* after perpetual adjustment

RISKS

Risks include, but are not limited to, unfavourable interest rate developments, unfavourable macroeconomic developments, and departure of key personnel.

COMPANY PROFILE

Grand City Properties is a specialist real estate company focused on investing in and managing value-add opportunities in the German real estate market. The overarching strategy is to improve the portfolio through targeted modernisation and intensive tenant management and thus create value by subsequently raising occupancy and rental levels.

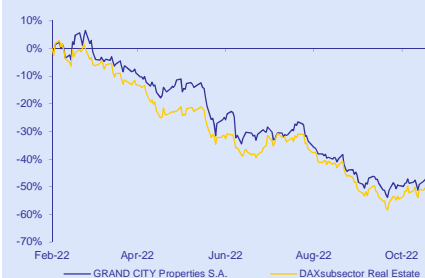
MARKET DATA

As of 16 Nov 2022

Closing Price	€ 10.51
Shares outstanding	176.18m
Market Capitalisation	€ 1851.65m
52-week Range	€ 8.79 / 22.44
Avg. Volume (12 Months)	325,730

Multiples	2020	2021	2022E
P/FFO 1	9.5	9.1	10.1
P/NTA	0.3	0.3	0.4
FFO 1 Yield	10.6%	10.9%	9.9%
Div. Yield	7.9%	8.2%	7.4%

STOCK OVERVIEW



COMPANY DATA

As of 30 Sep 2022

Liquid Assets	€ 386.50m
Investment properties	€ 9,729.80m
EPRA NTA	€ 5,242.80m
Total Assets	€ 11,287.60m
Current Liabilities	€ 372.80m
Total Equity	€ 6,029.90m

SHAREHOLDERS

Edolaxia Ltd.	59.0%
Treasury	2.0%
Free float	39.0%



THIRD QUARTER HIGHLIGHTS

Organic rental growth was driven by good operational performance leading to a 9.0% rise in net rent (NRI). The performance is traced to the combined impact of net acquisitions and solid like-for-like (LFL) performance between the two periods. Q3 NRI was close to our estimate (table 1).

The net acquisitions, closed mainly in H2/21 and H1/22, contributed to the 3.6% year-on-year increase in AEBITDA. However, the margin was around 230 basis points lower Y/Y at 78.3% on inflationary effects, mainly visible in higher personnel and service provider costs, that somewhat offset operational gains.

GCP realised total LFL net rental growth of 3.1% in the January-to-September period comprising 0.8% occupancy increases and 2.3% in-place rent. London, Berlin and Leipzig led the performance, but the company expects LFL rental growth to flatten out in 2023, as renters cope with soaring energy bills und tighter household budgets.

Table 1: Third quarter vs prior year and FBe

in €m	Q3/22	Q3/22E	Variance	Q3/21	Variance	9M/22	9M/21	Variance
Rental income	152	150	1.5%	131	15.9%	424	390	9.0%
Net rent	100	98	2.2%	93	7.7%	295	276	6.8%
Adjusted EBITDA	78	76	2.4%	75	4.3%	230	222	3.6%
margin	78%	78%	-	80%	-	78%	80%	-
FFO 1 (after perpetuals)	47	47	1.2%	46	2.6%	145	140	3.0%
FFOPS 1 (€) (after perpetuals)	0.28	0.28	1.2%	0.28	0.0%	0.87	0.84	3.6%

Source: First Berlin Equity Research; Grand City Properties

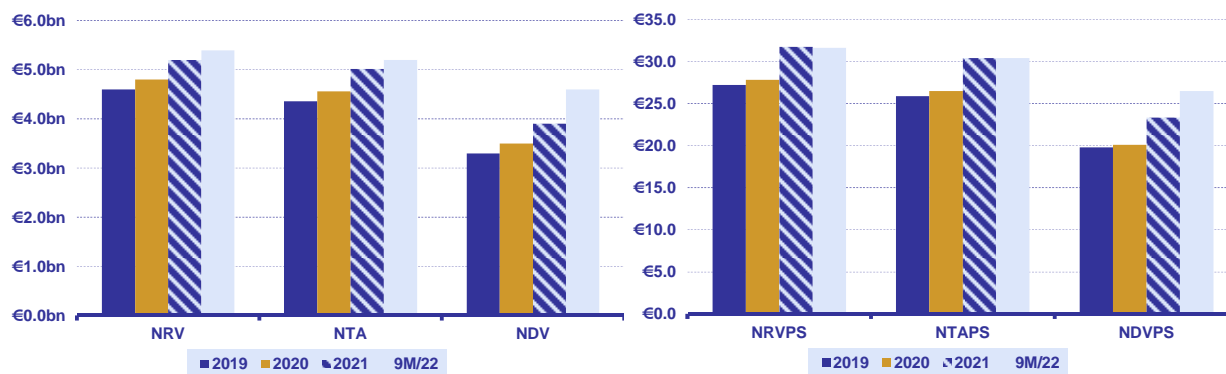
FFO 1, the key industry indicator for recurring operational cash flow, moved 3.0% higher Y/Y during 9M, while FFOPS 1 continues to benefit from share buyback effects (+3.6%) The Q3 performance was also in line with our estimate and has the company tracking well towards confirmed guidance and FBe. Annualised FFOPS 1 corresponds to a 10.7% yield. FFO 2 tallied €153m in 9M/22 with the transaction market largely stuck in a wait-and-see mode.

Revaluation gains softened in Q3 Property stocks have been under pressure most of the year, partly due to market fears that valuations, and thus NAVs, would greatly suffer in the higher interest rate environment. Grand City booked revaluation gains of €235m in 9M but only €126k in Q3 after reporting €189m for Q2/22. Around 80% of the portfolio was revalued for 9M reporting, and the balance is scheduled for Q4. We expect some devaluations in the October-to-December period and also now assume write-downs in 2023 with risk of up to 5% in line with management comments.



Portfolio value stable at €2,315 / m² In-place rent stood at €8.3 / m² at the end of 9M vs €8.1 / m² at YE21, while the portfolio vacancy rate dipped again Q/Q to a record low of 4.4% (H1/22: 4.7%). Valuation momentum has clearly stalled with the 'value / m²' indicator up a scant 0.8% sequentially. Annualised net rent tallied €397m at the end of 9M reporting.

Table 1: EPRA BPR reporting



Source: First Berlin Equity Research; Grand City Properties

Balance sheet stable Q/Q GCP used its solid liquidity position to redeem its €450m Series F convertible bonds and pre-pay around €165m of high interest bank loans in the nine month period.

Table 2: Financial highlights

in €m	9M/22	2021	Variance
Cash & liquid assets	387	1,108	-65%
Investment property	9,730	9,339	4%
Unencumbered assets	8,983	8,353	8%
Unencumbered assets ratio	90%	88%	-
Total equity	6,030	5,803	4%
EPRA NTA	5,243	5,020	4%
Loans and borrowings	252	358	-30%
Straight & convertible bonds	3,630	4,092	-11%
Loan-to-Value (LTV)	35%	36%	-
Equity ratio	53%	50%	-

Source: First Berlin Equity Research; Grand City Properties

The landlord has cash and liquid assets of around €387m—enough to cover debt maturities into mid-2025 with no maturities until Q2/24 (~€370m). Plus, GCP said it has access to another €300m in undrawn credit lines. Given the volatile refinancing environment, we reckon management will be patient in choosing the right refinancing structure.



Looming perpetual call dates GCP has several options for its perpetual notes callable in 2023. However, we now assume the notes will reset and factor in the higher interest payments, including 2.9% for the 5-year swap, into our forecasts. We note that only the reset notes will count as debt, while the others will continue to be recognised as equity. This reshuffling will not jeopardise the S&P credit rating. GCP brass said on the call that the reset option (-6.3% interest) is financially more prudent than refinancing at current market rates.

Table 3: Guidance vs FBe

	Unit	2022 Guidance	FBe 2022
FFO 1 (after perpetuals)	€m	188 -197	194
FFOPS 1 (after perpetuals)	€	1.13 - 1.18	1.15
DPS	€	0.85 - 0.89	0.86
LFL net rent growth	%	> 2.5	2.3
LTV	%	< 45	35

Source: First Berlin Equity Research; Grand City Properties

Guidance confirmed; FFOPS 1 growth of up to 6.3% Y/Y The company reported a solid Q3 close to our targets. Management thus reiterated 2022 guidance calling for FFOPS 1 (after perpetuals) of €1.13 to €1.18.

Figure 1: Changes to FBe and target price

	old	new	revision	upside	dividend yield	total upside
Price target (€)	19.0	16.8	-11.6%	59.8%	8.2%	68.1%
	2022E			2023E		
in €m	Old	New	Variance	Old	New	Variance
Net rent (NRI)	387	387	0.0%	405	395	-2.5%
AEBITDA	303	303	0.0%	318	298	-6.2%
margin (NRI)	78%	78%	-	78%	75%	-
FFO 1	194	194	0.0%	205	179	-12.9%
Margin	50%	50%	-	51%	45%	-
FFOPS 1 (€)	1.15	1.15	0.2%	1.19	1.04	-12.8%

Source: First Berlin Equity Research estimates

Lowering target price; staying at Buy We have dialled back our forecasts starting in 2023 to account for market headwinds. Changes include: (1) reset of the perpetuals callable in 2023; (2) an increase in property OpEx to track the latest inflationary effects; (3) higher current taxes to match latest run rates; (4) reduced LFL rental income growth for 2023 assuming only LFL occupancy growth (demand still well outpaces supply); and (5) property valuation write downs in Q4 and 2023. Our target price moves to €16.8 (old: €19).



VALUATION MODEL

	Unit	2022E	2023E	2024E	2025E	2026E	2027E	2028E	2029E	2030E	TV
FFOPS 1	€	1.15	1.04	1.05	1.11	1.04	1.00	0.96	0.94	1.01	1.02
Payout ratio	%	7.5	7.5	7.5	7.5	7.5	7.5	7.5	7.5	7.5	7.5
Dividend (DPS)	€	0.86	0.78	0.78	0.84	0.78	0.75	0.72	0.71	0.76	0.76
Y/Y	%		-0.10	0.01	0.06	-0.07	-0.04	-0.03	-0.02	0.07	n.a.
NPV	€	0.86	0.73	0.70	0.71	0.62	0.57	0.52	0.48	0.49	11.2
CAGR (2022 to 2026)	%	-1.4									
Terminal growth rate	%	1.0									
Discount rate	%	5.5									
NPV of dividends	€	5.7									
NPV of TV	€	11.2									
Fair value per share	€	16.8									

		Terminal growth						
		-0.5%	0.0%	0.5%	1.0%	1.5%	2.0%	2.5%
Discount rate	4.9%	15.2	16.3	17.6	19.3	21.4	24.3	28.5
	5.1%	14.7	15.7	16.9	18.4	20.3	22.8	26.3
	5.3%	14.2	15.1	16.2	17.6	19.3	21.5	24.5
	5.5%	13.8	14.6	15.6	16.8	18.4	20.3	23.0
	5.7%	13.4	14.1	15.1	16.2	17.5	19.3	21.6
	5.9%	13.0	13.7	14.5	15.5	16.8	18.3	20.4
	6.1%	12.6	13.3	14.0	15.0	16.1	17.5	19.3

		Cost of debt						
		2.25%	2.50%	2.75%	3.00%	3.25%	3.50%	3.75%
Discount rate	4.9%	22.4	21.4	20.3	19.3	18.3	17.2	16.2
	5.1%	21.3	20.3	19.4	18.4	17.4	16.4	15.5
	5.3%	20.3	19.4	18.5	17.6	16.7	15.7	14.8
	5.5%	19.5	18.6	17.7	16.8	16.0	15.1	14.2
	5.7%	18.6	17.8	17.0	16.2	15.3	14.5	13.7
	5.9%	17.9	17.1	16.3	15.5	14.7	14.0	13.2
	6.1%	17.2	16.5	15.7	15.0	14.2	13.5	12.7



INCOME STATEMENT

All figures in EURm	2018	2019	2020	2021	2022E	2023E
Net rent	364	383	372	375	387	395
Rental and operating income	545	560	535	525	540	581
Property revaluations & capital gains	507	401	343	695	202	-216
Result from equity-accounted investees	1	0	4	4	0	0
Property expenses	-261	-253	-226	-218	-225	-270
Cost of buildings sold	0	0	0	0	0	0
Administration expenses	-10	-11	-11	-11	-12	-12
Depreciation & amortisation	-3	-4	-5	-8	-6	-7
Operating income (EBIT)	780	693	640	986	499	76
Finance expenses	-46	-45	-53	-46	-43	-43
Other financial results	-36	-33	-46	-149	-42	0
Pre-tax income (EBT)	698	615	542	791	414	33
Current tax	-30	-37	-31	-39	-39	-42
Deferred tax	-85	-84	-61	-135	-33	36
Tax result	-115	-121	-93	-174	-73	-6
Minority interests	-64	-53	-54	-69	-34	-3
Hybrid note investors	-30	-33	-33	-25	-25	-33
Net income	489	407	362	524	283	-9
Basic EPS (€)	2.95	2.43	2.13	3.12	1.68	-0.05
AEBITDA	276	298	300	299	303	298
Ratios						
AEBITDA margin (% of net rent)	75.6%	77.8%	80.5%	79.7%	78.1%	75.5%
Tax rate	-10.8%	-12.5%	-10.5%	-13.1%	13.0%	14.0%
Expenses (% of net rent)						
Property expenses	71.7%	66.2%	60.8%	58.2%	58.0%	68.4%
Administration expenses	2.6%	3.0%	2.9%	3.0%	3.1%	2.9%
Y-Y Growth						
Rental and operating income	10.1%	2.8%	-4.4%	-2.0%	3.0%	7.6%
Total revenues	9.7%	2.8%	-4.4%	-2.0%	3.0%	7.6%
Operating income	-10.2%	-11.1%	-7.6%	54.0%	-49.4%	-84.8%
Adjusted EBITDA	11.1%	8.0%	0.7%	-0.4%	1.4%	-1.4%
Net income/ loss	-8.6%	-16.7%	-11.0%	44.5%	-46.0%	n.m.
Funds from Operations (FFO)						
Operating profit	780	693	640	986	499	76
Depreciation and amortisation	3	4	5	8	6	7
EBITDA	782	697	645	994	506	83
Property revaluations & capital gains	-507	-401	-343	-695	-202	216
Others	0	2	-2	-1	-1	-1
Adjusted EBITDA	276	298	300	299	303	298
Financial expense	-46	-45	-53	-46	-43	-43
Tax	-30	-37	-31	-39	-39	-42
Minorities	-2	-4	-1	-2	-2	-2
FFO 1 (before perpetuals)	198	212	215	211	219	212
Perpetual note adjustment	-30	-33	-33	-25	-25	-33
FFO 1	168	179	182	186	194	179
CapEx	-75	-76	-62	-63	-74	-49
AFFO	92	103	120	123	120	130





BALANCE SHEET

All figures in EURm	2018	2019	2020	2021	2022E	2023E
Current assets, total	1,238	1,629	2,264	1,679	1,034	1,154
Cash and cash equivalents	603	914	1,412	895	404	488
Traded securities at fair value though P&L	162	155	286	218	153	153
Trade and other receivables	319	342	395	452	466	502
Inventories - Trading property	17	16	16	0	0	0
Assets held for sale	136	201	155	114	11	11
Non-current assets, total	7,623	8,223	8,602	9,883	10,354	10,235
Equipment and intangible assets	24	27	27	70	77	85
Investment property	7,282	7,981	8,043	9,364	9,863	9,715
Equity accounted investees	26	21	108	0	0	0
Other LT assets	254	151	373	397	358	372
Deferred tax assets	37	42	51	51	57	62
Total assets	8,861	9,851	10,866	11,562	11,389	11,388
Current liabilities, total	306	454	427	773	336	387
Short-term debt	22	33	147	455	5	5
Trade and other payables	242	288	209	216	222	267
Other current liabilities	42	133	71	103	109	115
Long-term liabilities, total	3,887	4,431	4,884	4,986	4,989	5,084
Long-term debt	846	521	427	353	300	400
Convertible and straight bonds	2,450	3,195	3,639	3,642	3,657	3,679
Deferred taxes	523	592	634	760	794	758
Other LT liabilities	69	122	183	231	238	246
Minority interests	409	444	535	615	649	652
Shareholders' equity	4,258	4,523	5,020	5,188	5,415	5,266
Total consolidated equity and debt	8,861	9,851	10,866	11,562	11,389	11,388
Ratios						
EPRA NTA (€m)	n.a.	4,358	4,566	5,020	5,291	5,097
EPRA NTAPS (€)	n.a.	25.9	26.5	30.4	30.7	29.6
Net debt (€m)	2,560	2,690	2,521	3,342	3,405	3,444
Net debt / equity (x)	0.6	0.6	0.5	0.6	0.6	0.7
Net debt / EBITDA (x)	9.3	9.0	8.4	11.2	11.2	11.5
Interest cover (x)	6.0	6.6	5.7	6.4	7.1	6.9
Loan-to-value (LTV)	34%	33%	31%	36%	35%	35%
Equity ratio	53%	50%	51%	50%	53%	52%
Return on equity (ROE)	12.5%	9.9%	8.1%	10.6%	5.6%	0.5%



CASH FLOW STATEMENT

All figures in EURm	2018	2019	2020	2021	2022E	2023E
Net income	583	493	449	617	342	27
Depreciation and amortisation	3	4	5	8	6	7
Profit from equity accounted investees	-1	0	-4	-4	0	0
Change in fair value of investment properties	-507	-401	-343	-695	-202	216
Net finance expenses	82	78	98	195	85	43
Tax result	115	121	93	174	73	6
Others	1	2	2	3	0	0
Operating cash flow	276	298	300	299	304	299
Change in working capital	-23	-20	-29	-45	0	18
Tax paid	-28	-28	-28	-37	-39	-42
Net cash flow from operating activities	225	249	242	217	265	276
Investment in fixed/intangible assets	-6	-7	-7	-8	-14	-15
Net property investments / disposals	-501	-194	-492	-465	-195	-69
Acquisition of subsidiaries	-112	31	547	333	0	0
Proceeds from investments in financial assets	-100	117	-439	-58	105	-14
Cash flow from investing	-718	-53	-392	-198	-103	-98
Debt financing, net	916	360	559	-71	-488	122
Equity financing, net	312	-33	207	-91	-25	-25
Share buyback	0	0	0	-272	0	0
Dividend paid	-79	-107	-71	-54	-55	-149
Other financing activities	-306	-55	7	0	-42	0
Net paid financing expenses	-56	-50	-51	-50	-43	-43
Cash flow from financing	785	115	651	-537	-653	-94
Fx effects	-1	0	-3	2	0	0
Net cash flows	291	311	498	-517	-491	84
Cash, start of the year	312	603	914	1,412	895	404
Cash, end of the year	603	914	1,412	895	404	488
AEBITDA / share (€)	1.65	1.77	1.74	1.69	1.65	1.63
FFO 1*	168	179	182	186	194	179
FFOPS 1* (€)	1.01	1.07	1.07	1.11	1.15	1.04
Y-Y Growth						
Operating cash flow	11.0%	11.1%	-2.9%	-10.4%	22.0%	4.3%
Adjusted EBITDA / share	9.8%	7.3%	-1.6%	-2.8%	-2.7%	-1.4%
FFO 1	9.0%	6.8%	1.8%	2.3%	4.1%	-7.8%
FFOPS 1	5.0%	5.8%	0.3%	3.6%	3.5%	-9.9%

* adjusted for perpetual notes

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Anschrift:

First Berlin Equity Research GmbH
Mohrenstr. 34
10117 Berlin
Germany

Vertreten durch den Geschäftsführer: Martin Bailey

Telefon: +49 (0) 30-80 93 9 680

Fax: +49 (0) 30-80 93 9 687

E-Mail: info@firstberlin.com

Amtsgericht Berlin Charlottenburg HR B 103329 B

UST-Id.: 251601797

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First Berlin Equity Research GmbH

Authored by: Ellis Acklin, Senior Analyst

All publications of the last 12 months were authored by Ellis Acklin.

Company responsible for preparation: First Berlin Equity Research GmbH, Mohrenstraße 34, 10117 Berlin

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Person responsible for forwarding or distributing this financial analysis: Martin Bailey

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PRICE TARGET DATES

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The present financial analysis is based on the author's own knowledge and research. The author prepared this study without any direct or indirect influence exerted on the part of the analysed company. Parts of the financial analysis were possibly provided to the analysed company prior to publication in order to avoid inaccuracies in the representation of facts. However, no substantial changes were made at the request of the analysed company following any such provision.

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First Berlin's system for asset valuation is divided into an asset recommendation and a risk assessment.

ASSET RECOMMENDATION

The recommendations determined in accordance with the share price trend anticipated by First Berlin in the respectively indicated investment period are as follows:

Category		1	2
Current market capitalisation (in €)		0 - 2 billion	> 2 billion
Strong Buy ¹	An expected favourable price trend of:	> 50%	> 30%
Buy	An expected favourable price trend of:	> 25%	> 15%
Add	An expected favourable price trend of:	0% to 25%	0% to 15%
Reduce	An expected negative price trend of:	0% to -15%	0% to -10%
Sell	An expected negative price trend of:	< -15%	< -10%

¹ The expected price trend is in combination with sizable confidence in the quality and forecast security of management.

Our recommendation system places each company into one of two market capitalisation categories. Category 1 companies have a market capitalisation of €0 – €2 billion, and Category 2 companies have a market capitalisation of > €2 billion. The expected return thresholds underlying our recommendation system are lower for Category 2 companies than for Category 1 companies. This reflects the generally lower level of risk associated with higher market capitalisation companies.

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The First Berlin categories for risk assessment are low, average, high and speculative. They are determined by ten factors: Corporate governance, quality of earnings, management strength, balance sheet and financial risk, competitive position, standard of financial disclosure, regulatory and political uncertainty, strength of brandname, market capitalisation and free float. These risk factors are incorporated into the First Berlin valuation models and are thus included in the target prices. First Berlin customers may request the models.

RECOMMENDATION & PRICE TARGET HISTORY

Report No.:	Date of publication	Previous day closing price	Recommendation	Price target
Initial Report	21 January 2013	€4.37	Buy	€14.30
2...43	↓	↓	↓	↓
44	15 April 2021	€22.26	Buy	€27.50
45	19 May 2021	€21.88	Buy	€27.50
46	17 August 2021	€23.40	Buy	€27.50
47	16 November 2021	€22.28	Buy	€28.00
48	18 March 2022	€19.92	Buy	€28.00
49	18 May 2022	€16.43	Buy	€24.50
50	16 August 2022	€13.86	Buy	€24.00
51	12 October 2022	€9.29	Buy	€19.00
52	Today	€10.51	Buy	€16.80

INVESTMENT HORIZON

Unless otherwise stated in the financial analysis, the ratings refer to an investment period of twelve months.

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Legally required information regarding

- key sources of information in the preparation of this research report
- valuation methods and principles
- sensitivity of valuation parameters

can be accessed through the following internet link: <https://firstberlin.com/disclaimer-english-link/>

SUPERVISORY AUTHORITY: Bundesanstalt für Finanzdienstleistungsaufsicht (German Federal Financial Supervisory Authority) [BaFin], Graurheindorferstraße 108, 53117 Bonn and Marie-Curie-Straße 24-28, 60439 Frankfurt am Main

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